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In The

Supreme Court of the United States

October Term, 1986

CHICAGO SYSTEMS SOFTWARE, and BRIAN BRAZDA, an individual, and JAMES M. DAVEY, and individual, d/b/a CHICAGO SYSTEMS SOFTWARE,

Petitioners,

vs.

EVANS NEWTON, INCORPORATED,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT AND APPENDIX

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QUESTIONS PRESENTED FOR REVIEW

1. Whether a copyrighted work can ever be a "work made for hire" under subsection (1) of the definition of that term in 17 U.S.C. §101 (1985), where the work is specially ordered or commissioned and created by an independent contractor, and where the parties did not expressly agree in a written instrument signed by them that the work shall be considered a "work made for hire".

2. Whether the Seventh Circuit violated Rule 52(a), F.R.C.P., by making what it perceived to be an essential factual finding of "supervision" in deciding the "work made for hire" issue and by affirming a damage award, despite recognizing that the District Court failed to specify both a factual and legal basis for the award.

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Petitioners,

vs.

EVANS NEWTON, INCORPORATED,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Petitioners, Chicago Systems Software, Brian Brazda, and James M. Davey respectfully pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Seventh Circuit, entered in this proceeding on June 19, 1986, affirming in part and reversing in part the judgment of the United States District Court for the Northern District of Illinois.

OPINIONS BELOW

The Court of Appeals affirmed the District Court's grant of an injunction and its award of $16,000 in actual damages to Plaintiff-Respondent, and reversed the award of attorney's fees and punitive damages. The opinion and judgment of the Appellate Court is made part of the Appendix attached to this Petition. The Opinion of the Court of Appeals is reported at 793 F.2d 889 (7th Cir. 1986).

The original action was tried in the United States District Court for the Northern District of Illinois. On September 11, 1984. the District Court awarded plaintiff $16,000 in unspecified damages, $16,000 in exemplary damages, and costs and attorneys fees. On October 29, 1984 the District Court amended certain of its findings. On February 27, 1985, the District Court entered an order awarding plaintiff $16,000 in attorney's fees. The opinion of the District Court including its amended findings is attached hereto as part of the Appendix.

JURISDICTION

This Petition for a Writ of Certiorari is being filed within ninety (90) days of the entry of the judgment of the Court of Appeals, on June 19, 1986.

The jurisdiction of this Court is based upon 28 U.S.C. §§1254(1) and 2101(c).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Article I, Section 8 of the U.S. Constitution provides that:

> The Congress shall have Power . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.

Copyright Act of 1976, Sections 101 and 201(b) provide that:

Sec. 101. Definitions

As used in this title, the following terms and their variant forms means the following:

* * *

A "work made for hire" is - -

(1) a work prepared by an employee within the scope of his or her employment; or

(2) a work specially ordered or commissioned for use as a contribution to a collective work, as a part of a motion picture or other audiovisual work, as a translation, as a supplementary work, as a compilation, as an instructional text, as a test, as answer material for a test, or as an atlas, if the parties expressly agree in a written instrument signed by them that the work shall be considered a work made for hire. For the purpose of the foregoing sentence, a "supplementary work" is a work prepared for publication as a secondary adjunct to a work by another author for the purpose of introducing, concluding, illustrating, explaining, revising, commenting upon, or assisting in the use of the other work, such as forewords, afterwords, pictorial illustrations, maps, charts, tables, editorial notes, musical arrangements, answer material for tests, bibliographies, appendixes, and indexes, and an "instructional text" is a literary, pictorial, or graphic work prepared for publication and with the purpose of use in systematic instructional activities.

Section 201. Ownership of Copyright

(b) Works Made for Hire. - - In the case of a work made for hire, the employer or other person for whom the work was prepared is considered the author for purposes of this title, and, unless the parties have expressly agreed otherwise in a written instrument signed by them, owns all of the rights comprised in the copyright.

STATEMENT OF THE CASE

This case involved alleged copyright infringement, misappropriation of trade secrets, unfair competition and breach of contract relating to Plaintiff Evans Newton Incorporated's (ENI) microcomputer program and user's manual therefor. These materials were designed for use by educational institutions, and together were entitled "Project Basic". The computer program was written entirely by the defendants (jointly referred to as CSS) for ENI. Documentation upon which the user's manual was based in part was written by CSS and provided to ENI. ENI subsequently "rewrote" and "reedited" these "preliminary drafts" of CSS' documentation to prepare the final copyrighted manual (Ferguson Dep. p. 76).[1]

ENI was in the business of providing educational institutions with recordkeeping systems for storing student grades, student progress in the classroom, and other similar information and for producing report cards and other pertinent reports (F 5,6). CSS provided computer programming services and was hired by ENI in 1979 to assist with Project Basic (F 8). Defendants were "independent contractors hired because of their pre-existing expertise in the field of educational programs" (CL 16). In May 1979, ENI was referred to CSS as a source for computer programming skills because ENI wanted to incorporate computer technology into recordkeeping systems and develop a "computer managed instructional" (CMI) system (F 8). CSS had developed "its own version of a class-

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[1] The following abbreviations are used:

A: Appendix to Petition for Writ of Certiorari.

F: Finding of Fact of the District Court, Judgment of September 11, 1984, as amended by the Court's Order of October 29, 1984.

CL: Conclusion of Law of the District Court, Judgment of September 11, 1984, as amended by the Court's Order of October 29, 1984.

Dep.: Deposition transcript of the page indicated.

Tr: Trial Transcript.

room management program in about April 1979" and showed a "demonstration version" to ENI and its customers in May 1979 (F 9).

Shortly after the demonstration, ENI sent CSS "system bid guidelines", also called "bid specifications", including flow diagrams, numbering and coding systems, and sample printouts and reports (F 7), for the purpose of soliciting CSS' cost estimate for its services. In June CSS submitted its bid of $5,500 to provide the programming, including complete documentation for the system (F 8). The bid was accepted, and work began with a deadline in August 1979 (F 10). On August 6, 1979 ENI wrote to CSS setting forth "terms of this commitment" including: "6. The ENI Copyright of this program is fully recognized by Chicago Software Systems [sic]" (F 10).

In August 1979, CSS travelled to Phoenix at its own cost to demonstrate the program and deliver the documentation (F 10). At the conclusion of the demonstration, ENI presented to CSS and CSS signed an "ENI Microcomputer Program Copyright Statement", which stated in part that "all Microcomputer Programming done by [CSS] . . . for [ENI] . . . is the exclusive property of ENI", and that CSS agrees "not to sell . . . programs written for ENI to [others]". Then CSS was paid the first $1,500 of its fee (F 11).

The parties' relationship degenerated thereafter, with ENI delaying further payments to CSS because of alleged deficiencies in the program. In April 1980, ENI began marketing the Project Basic program (F 12). On June 13, 1980, ENI received a copyright registration on its manual as an unpublished work, and the certificate of registration stated that it was a "work made for hire" (F 13).

After terminating its relationship with ENI in late 1979, CSS resumed work on its own CMI system and, beginning in April 1980, CSS marketed a competitive program and user's manual (F 14). In connection with preparing its manual, CSS

referred to the documentation provided to ENI (Tr 640), but not to the copyrighted manual because CSS did not have access to it. CSS sold only two complete copies of its system for a total of $1,200, and several demonstration versions for which it received less than $200. One of CSS' sales went to Omega Business Products, Inc., a firm asked by ENI to purchase CSS' system for ENI's investigation and at ENI's cost (Tr 115,642).

ENI filed a Complaint in the U.S. District Court for the District of Arizona in March 1981, basing jurisdiction on 28 U.S.C. §1338. The case was transferred to the U.S. District Court for the Northern District of Illinois upon CSS' motion. At the bench trial, ENI asserted infringement of its copyrights on the program and on the manual, but the program claim was dismissed because ENI failed to prove that it had registered a copyright for the program in suit (A 10a, n.6). The District Court found infringement of the manual copyright, stating that "[m]aterial portions of [CSS'] manual have substantial similarity to [ENI's] manual" (F 16). The similarity was based on the documentation submitted by CSS and incorporated in ENI's manual. No evidence was presented and no findings were made that CSS had access to any portion of ENI's manual created by ENI since the manual was an unpublished work at the time CSS began marketing its own manual.

Also concluding that CSS engaged in unfair competition and violation of a confidentiaility agreement (CL 24) (presumably based on the aforesaid "ENI Copyright Statement"), the District Court awarded an injunction and $16,000 in unspecified damages, $16,000 in exemplary damages, and $16,000 in attorneys' fees. The only findings on damages made by the district court were that: ENI obtained 60 out of a possible 300 dealers as customers, who each paid ENI between $10,000 and $25,000; and that ENI made unsuccessful efforts to sell its system in seven states, but ENI's lack of success "was not shown to be due to confusion in the market place caused by [CSS]" (F 20).

On appeal, the Seventh Circuit reversed the awards of

exemplary damages and attorneys' fees. Viewing the unfair competition and violation of confidentiality agreement as "alternate theories [which] are merely additional grounds to support the court's decision" (A 11a), the Appellate Court affirmed the award of $16,000 in unspecified damages on the basis that CSS infringed the copyright on the manual. In so doing, the Seventh Circuit held that even though the District Court found CSS to be an independent contractor, it was also an "employee" within the meaning of the "work made for hire" provisions of the 1976 Copyright Act, 17 U.S.C. §101. Therefore, instead of being a co-author and co-owner of the copyright in the documentation it wrote for ENI, CSS was an infringer of ENI's copyright when CSS used that documenation for its own manual.

REASONS FOR GRANTING THE WRIT

I. The Seventh Circuit Court Of Appeals Decision Improperly Expands The "Work Made For Hire" Doctrine And Subverts The Intent Of Congress In Enacting The Copyright Act Of 1976

The Seventh Circuit has held in this case that an "independent contractor" hired to create a copyrighted work can also be an "employee" within the meaning of the "work made for hire" provision of the Copyright Act, 17 U.S.C. §101 (1985), so as to vest copyright ownership in the employer rather than in the independent contractor. 17 U.S.C. §201(a)(1985). With this decision, the Seventh Circuit has unraveled over 15 years of Congressional work and debate focused, at least in part, on revising and changing this particular area of copyright law.

The Seventh Circuit framed the issue as follows:

> Whether CSS was an employee of ENI for purposes of 17 U.S.C. §101 turns upon whether Congress intended the term employee to encompass only "regular" employees as CSS contends, or whether Congress intended the 1976 Act to retain the some-

what more flexible definition of employee under the 1909 Copyright Act.

(A 8a).

In fact, however, the 1909 Copyright Act did *not* define or even use the term "employee". It defined "author" to include "an employer in the case of works made for hire". 17 U.S.C. §26 (1952). But the 1909 Act did not define "work made for hire". Judicial construction of that phrase created a presumption that an employer or commissioning party was the copyright owner of all works created or prepared by employees or by independent contractors, unless there was evidence to the contrary. *May v. Morganelli-Heumann & Associates*, 618 F.2d 1363, 1368 (9th Cir. 1980).

The legislative history of the Copyright Act of 1976 indicates that Congress intended to *change* the then existing copyright law and not merely codify the case law developed under the Copyright Act of 1909. H.R. Rep. 94-1476, 94th Cong., 2d Sess., 47-50 (1976), *reprinted in U.S. Code Cong. & Ad. News* 5659, 5660-63 (1976). One significant change was made in the area of "works made for hire", which was statutorily defined in section 101 of the new Act.

This Court has never construed the "work made for hire" provision of the 1976 Act. Its importance to all persons engaged in copyright activities is illustrated by the years of Congressional debate described herein. The Seventh Circuit's decision here injects substantial uncertainty in the law, not only as to copyright ownership, but also as to the consequences of "work made for hire" status under other provisions of the Copyright Act. 17 U.S.C. §§203 (termination of copyright transfers) and 302(c) (duration of copyright). Thousands of independent contractors relying on the law, as seemingly clearly expressed in the statute, now may not be adequately protected by contract as a result of the distorted statutory interpretation adopted by the Seventh Circuit. Likewise, employers should know once and for all when a "work made for hire" contract

is needed and when it is not. The Seventh Circuit's interpretation of the statute breaks down the clear boundaries for "works made for hire" and creates a vast area of uncertainty as to what constitutes a "work made for hire." This judicially created vagueness will eventually result in extensive litigation on this issue with its consequent inordinate burden on creators of copyrighted works.

When revision of the 1909 Copyright Act began, early debate centered on whether specially ordered or commissioned works should be excluded entirely from the "work made for hire" doctrine. A 1960 study prepared for the Copyright Office in connection with revision of the law characterized the then existing state of the "work made for hire" law as follows:

> Hence it may be concluded that section 26 refers only to works made by salaried employees in the regular course of their employment.

Patry: Latman's The Copyright Law p. 118 (BNA Books 6th ed. 1986), citing from Varmer, "Works Made for Hire and on Commission", *Copyright Office Study No. 13,* 86th Cong., 2d Sess. 130 (Comm. Print 1960).

The courts, however, did not uniformly limit application of the "work for hire" doctrine to salaried employees. The "statutory concept of employment for hire" was expanded through the common law to situations where the creative party was an independent contractor whose work was specially ordered or commissioned. See *Brattleboro Publishing Co. v. Winmill Publishing Corp.*, 369 F.2d 565 (2d Cir. 1966), and additional cases cited in Nimmer, *Nimmer On Copyright* §5.03 [B](2) at 5-21 n. 60 (1985). In those cases, the courts frequently attempted to ascertain the intention of the parties; but, when that was not possible, a presumption was created that the commissioning party was both the author and copyright owner. This presumption became the legal equivalent to the "work made for hire" doctrine applied to employers and employees. Thus, during the copyright law revision efforts, a major battleground formed around the

"work made for hire" provision, where authors, composers and artists opposed literary and music publishers and motion picture studios.

In 1961, the Register of Copyrights issued a Report discussing the copyright ownership of commissioned works:

> The phrase used in the present (1909) statute -- "works made for hire" -- has been criticized as being inexact, *because it might be thought to include works made on special commission.* The courts, however, have not generally regarded commissioned works as "made for hire."
>
> * * *
>
> Instead of the phrase "works made for hire," it was proposed in previous revision bills to substitute "works created by an employee within the regular scope of his employment." We would adopt this *more precise language* as a definition of "works made for hire" (emphasis added).

Report of the Register of Copyrights on the General Revision of the U.S. Copyright Law, 87th Cong., 1st Sess. 85, 86-87 (1961).

The distinction between an employee and those persons "specially commissioned" is further emphasized by a preliminary draft bill from the Copyright Office in 1963, which defined a "work made for hire" as "a work prepared by an employee within the scope of the duties of his employment, *but not including a work made on special order or commission"* (emphasis supplied). *Supplementary Report Of the Register of Copyrights On The General Revision Of The U.S. Copyright Law,* 89th Cong., 1st Sess. 66 (Comm. print 1965).

This language evidences an intention *not* to grant "work made for hire" status to specially ordered or commissioned works, and to separate persons creating such works from "employees". Nevertheless, this definition was strongly opposed by book publishers and the like, whose work involved translations, maps and illustrations, which are often prepared

on special order or commission, but which by their very nature should be treated as "works made for hire." It was also opposed by persons involved with music and choreography, which were also works frequently prepared on special order or commission and incorporated in other creative works. Accordingly, "the problem was how to draw the proper definitional line." *Id.* at 67.

The 1964 bill attempted to solve this problem by including in the definition of a "work made for hire", "a work prepared on special order or commission if the parties expressly agree in writing that it shall be considered a work made for hire." *Id.* at 67. Author's organizations objected to this approach because authors could be easily induced into signing form "work made for hire" contracts, and because regular book publishing contracts could be converted into "employment agreements." The 1965 bill attempted to resolve this conflict by defining a "work made for hire" as:

> (1) a work prepared by an employee within the scope of his employment; or (2) a work specially ordered or commissioned for use as a contribution to a collective work, as a part of a motion picture, as a translation, or as a supplementary work, if the parties expressly agree in writing that the work shall be considered a work made for hire.

Supplementary Report of the Register of Copyrights on the General Revision of the U.S. Copyright Law, 89th Cong., 1st Sess., 67 (Comm. print 1965). A 1965 Report from the Register of Copyrights stated:

> The thought here is that, in the four special cases specifically mentioned (contributions to collective works and motion pictures, translations, and supplementary works), the work will be considered a "work made for hire," but only if it is in fact specially ordered or commissioned" for that purpose and if there is an express agreement in writing that the work be considered "made for hire". *Other works made on special order or commission would not come within the definition.* (emphasis added).

Supplementary Report at 67-68.

In 1966, five more categories were added to those specially ordered or commissioned works which could be considered "works made for hire." A House Report issued just prior to enactment of the final bill noted that the status of works prepared on special order or commission was "a major issue" in the development of the definition of "works made for hire." It also stated:

> The basic problem is how to draw a statutory line between those works written on special order or commission that should be considered as "works made for hire," and those that should not. The definition [of "works made for hire"] . . . represents a compromise which, in effect, spells out those specific categories of commissioned works that can be considered 'works made for hire' under certain circumstances.

H.R. Rep. 94-1476, 94th Cong., 2d Sess. 121, *reprinted in* 1976 *U.S. Code Cong. & Ad. News* 5659, 5736.

Thus, by enacting the presently worded statute, Congress intended to limit the specially ordered or commissioned works eligible for "work made for hire" status to those fulfilling the requirements delineated in subsection 2 of the definition set forth in 17 U.S.C. §101.

The Seventh Circuit's holding that the work of an independent contractor can be a "work made for hire" under the "employee" category of the "work made for hire" doctrine blurs the distinction between subsections (1) and (2) of the definition of this term under 17 U.S.C. §101 (1985). The holding contravenes Congressional intent, constitutes a return to the law as it existed prior to the effective date (January 1, 1978) of the 1976 Act, and threatens the rights of those independent authors, composers, and artists who worked to revise the prior law. This holding also is inconsistent with cases like *May v. Morganelli-Neumann & Associates,* 618 F.2d 1363 (9th Cir. 1980), and *Melter v. Zoller,* 520 F. Supp. 847 (D.N.J. 1981), which viewed the 1976 Act as a substantial

change to the "work made for hire" law and a limitation upon the types of specially ordered or commissioned works which can be "works made for hire."

The Seventh Circuit failed to recognize that the Copyright Act does not permit the work of an independent contractor to be classified as a "work made for hire" *unless* it qualifies as a "specially ordered or commissioned" work. To hold otherwise is to emasculate the careful limitations set forth in subsection (2) of the "work made for hire" provision, and to permit recapture under subsection (1) of all of the works excluded by subsection (2).

The Seventh Circuit's *sole* support for its enormously significant decision was the Second Circuit's opinion in *Aldon Accessories v. Spiegel Inc.*, 738 F.2d 548 (2d Cir.), *cert. denied* ___U.S.___, 105 S.Ct. 387 (1984) (A 8a-9a). This reliance on *Aldon* is misplaced. To the extent that *Aldon* is construed as support for the proposition that works of independent contractors can be considered "works made for hire" under the "employee" portion of section 101, *Aldon* "turns the work for hire provision inside out". FitzGibbon and Kendall, "The Unicorn in the Courtroom: The Concept of Supervising and Directing an Artistic Creation Is a Mythical Beast in the Copyright Law," 15 *Journal of Arts Management and Law* 23, 40 (Fall 1985). *Aldon* has created a storm of controversy, as illustrated by 1 *The Copyright Law Journal* 38, 39 (October 1984), and a bill to amend the law regarding "work made for hire", S. 2330, 99th Cong. 2d Sess, introduced by Senator Cochran to the Committee on the Judiciary on April 17 (legislative day, April 8), 1986. Both *Aldon* and the present decision of the Seventh Circuit overlook Congress' intention that works which are specially ordered or commissioned should not generally be considered "works made for hire."

But *Aldon* need not be so broadly construed. The facts there justify the decision on a legal basis other than "work made for hire." Aldon's principal, Ginsburg, sent his Japanese

designer, who was not a regular employee of Aldon, a sketch of the pose he desired for the statuette in issue, and later traveled to Japan to work with artists hired by the Japanese company. "The gist of his testimony was that while he is not an artist and did not do the sketching or sculpting, he actively supervised and directed the work step by step," 738 F.2d at 550, and he "stood over the artists . . . telling them exactly what to do." 738 F.2d at 553. With this kind of close involvement, both prior 1976 law and current law could have found Ginsburg to be *the creator and sole author of the work, or at least a co-author, without resort to the "work made for hire" provision. See, Edward B. Marks Music Corp. v. Jerry Vogel Music Co.*, 140 F.2d 266 (2d Cir. 1944), and *Shapiro, Bernstein & Co. v. Jerry Vogel Music Co.*, 161 F.2d 406 (2d Cir. 1946), *cert. denied* 331 U.S. 820 (1947), decided under the old copyright law, and 17 U.S.C. §101 (1985), defining a "joint work" under the current law.

In contrast, in the present case the District Court made *no* findings of supervision or direction by ENI, and there was no evidence of such. ENI merely provided "bid specifications" to CSS to permit it to submit a cost estimate, and CSS then prepared the documentation. ENI could not have been the creator of the documentation. ENI, located in Phoenix, exercised no supervision or direction over CSS, located in Chicago, during CSS' preparation of this documentation (which later became a portion of ENI's manual). CSS furnished its own employees, computers and offices, traveled to Arizona at its own cost (F 10), and was paid a lump sum (without withholding taxes) based upon an estimate of time to be spent (F 8). CSS' work was not created initially at ENI's request; the District Court found that CSS "already had similar materials" when ENI delivered its bid specifications to CSS *before* CSS was retained (CL 16). The Seventh Circuit inexplicably stated that "[t]he evidence at trial essentially came down to a credibility contest" and the "[district] judge believed ENI's testimony that Ferguson supervised and directed the work" (A 9a), but no such contest or testimony

actually occurred. The course of events between the retention of CSS by ENI and CSS' delivery of documentation was not disputed at trial.

The Seventh Circuit should have held that CSS was a co-author of the copyrighted manual, because CSS' own documentation was incorporated into the manual, and that documentation formed the basis for the finding of substantial similarity. CSS was not an "employee" as that term has been defined by any prior authority. *See, Restatement of Agency 2d* 220, distinguishing between a "servant" and an "independent contractor"; *Epoch Producing Corporation v. Killiam Shows, Inc.*, 522 F.2d 737, 745 (2d Cir. 1975), *cert. denied* 424 U.S. 955 (1976) (existence of copyrighted work prior to existence of corporate employer contradicts "work made for hire"); and *Aitken, Hazen, Hoffman, Miller, P.C. v. Empire Construction Company*, 542 F. Supp. 252, 258 (D. Neb. 1982) (right to direct result does not equal the right to control and direct the detail and means to create the result).

II. The Seventh Circuit, Contrary To Rule 52(a) F.R.C.P., Made Its Own Findings Of Fact To Justify Its Decision And The Decision Of The District Court

Rule 52(a), F.R.C.P. requires that in all actions tried without a jury, the District Court "shall find the facts specially and state separately its conclusions of law thereon. . . ."

In this case, the Seventh Circuit conducted a *de novo* review of the record and made two of its own factual findings to justify a partial *affirmance* of the District Court's opinion. Since this Court has recently considered the impropriety of a *de novo* review in connection with a *reversal* of a district court's decision, *Anderson v. City of Bessemer City, N.C.*,___U.S.___, 105 S. Ct. 1504 (1985), it should now take this opportunity to examine and reject the same procedure still being utilized in connection with affirmances.

The Seventh Circuit made two critical factual findings on

its own, one more candidly than the other. First, the Seventh Circuit found on its own that ENI supervised and directed CSS. The District Court made no such finding, but that finding was the linchpin to the Seventh Circuit's conclusion that the copyrighted work was a "work made for hire." Second, the Seventh Circuit concluded that "[t]he record contains sufficient support" for the District Court's award of $16,000 in damages (A 13a), even though the Seventh Circuit admitted that its "analysis of this issue is complicated by the fact that the District Court did not make it clear whether the damages were actual or statutory, or what the basis for the $16,000 amount was" (A 11a-12a). The Appellate Court was forced to speculate on the basis for this award, stating that "perhaps [it was] based upon what ENI would have profited. . . ." (A 13a). For the Appellate court to determine that "the record contains sufficient support" for the award without understanding the District Court's legal or factual *basis* for it, implicitly requires impermissible fact finding. Indeed, the District Court provided no basis or findings to support the award, and even ENI failed to offer an explanation on appeal.

This Court has stated that:

> The reviewing court oversteps the bounds of its duty under Rule 52 if it undertakes to duplicate the role of the lower court . . . [A]ppellate courts must constantly have in mind that their function is not to decide factual issues *de novo*.

Anderson v. City of Bessemer City, N.C.,___U.S.___, 105 S.Ct. 1504, 1511-12 (1985), *quoting Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100 (1969). Where the trial court fails to make findings, or to find on a material issue, and an appeal is taken, the appellate court should remand the action so that appropriate findings can be made. The same is true when the findings are merely conclusory statements and do not fully address the issues raised in the litigation. J. Moore, 5A *Moore's Federal Practice* ¶52.06 [2] (2d ed. 1986). An appellate court should not attempt to resolve

factual issues in its own, *Rule v. International Association of Bridge, Structural and Ornamental Ironworkers, Local Union No. 396,* 568 F.2d 558, 568 (8th Cir. 1977), but should remand the case to the district court for appropriate findings.

> [F]act finding is the basic responsibility of district courts, rather than Appellate Courts, and . . . the Court of Appeals should not have resolved in the first instance this factual dispute which had not been considered by the District Court.

DeMario v. U.S., 415 U.S. 449, 450 (1974). *See also Pullman-Standard v. Swint,* 456 U.S. 273, 291-292 (1982).

This last principle is particularly applicable to the Seventh Circuit's "work made for hire" analysis. There was no finding by the District Court upon which the Appellate Court could have determined that CSS was "directed and supervised" by ENI. The District Court found CSS to be "independent contractors" and the copyrighted manual to be a "work made for hire", but it made no effort to square the former with the latter. Nor did the parties ever argue the supervision issue, until the Seventh Circuit raised it at the oral argument. The supervision issue was decided *de novo* on appeal. Regarding the damage award, the Seventh Circuit was unable to do more than speculate on the District Court's conclusory finding. If there are insufficient findings to justify a decision other than by speculation, Rule 52 and the previously cited decisions mandate that the decision be reversed or vacated and remanded for further findings on these issues. Because the Appellate Court did not do so, it committed reversible error. The Seventh Circuit's procedure has broad implications on the scope of appellate review and should be considered and clarified by this Court.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should issue.

Respectfully submitted,

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APPENDIX

In the

United States Court of Appeals

For the Seventh Circuit

No. 84-2971

EVANS NEWTON INCORPORATED, a New Jersey corporation,

Plaintiff-Appellee,

v.

CHICAGO SYSTEMS SOFTWARE, and BRIAN BRAZDA, an individual, and JAMES M. DAVEY, an individual, d/b/a CHICAGO SYSTEMS SOFTWARE,

Defendants-Appellants.

Appeal from the United States District Court
for the Northern District of Illinois, Eastern Division.
No. 81 C 3564—**Thomas R. McMillen**, *Judge.*

ARGUED DECEMBER 6, 1985—DECIDED JUNE 19, 1986

Before CUMMINGS, *Chief Judge*, and WOOD, JR., and CUDAHY, *Circuit Judges.*

WOOD, JR., *Circuit Judge.* This case involves allegations that the defendants Chicago Systems Software, Brian Brazda, and James Davey engaged in copyright infringement, misappropriation of trade secrets, unfair competition, and breach of contract, based upon the defendants' alleged improper copying of the plaintiff Evans Newton Incorporated's user's manual for the microcomputer program "Project Basic." The plaintiff contracted with the defendants for the defendants to do the computer programming for Project Basic, a program used by educa-

tional institutions. The defendants, after finishing work for the plaintiff, attempted to market their own manual and computer program to compete with Project Basic.

The plaintiff consequently sued for damages and to enjoin the defendants from marketing the competing program. The defendants counterclaimed that the plaintiff had impermissibly interfered with the defendants' attempts to market their own manual and program. A bench trial before Judge McMillen resulted in a verdict for the plaintiff. Defendants appeal a number of factual findings and conclusions of law. We affirm in part but reverse the district court's award of punitive damages and the plaintiff's attorneys' fees.

I. FACTS

The district court found the following to be the facts of this case. The plaintiff, Evans Newton Incorporated ("ENI"), is a corporation which provides recordkeeping systems to educational institutions throughout the country. During 1978, ENI decided to adapt its educational instruction program to programmable calculators. In cooperation with Victor Business Products, ENI developed calculator-managed and assisted programs for use with the Victor 4900 programmable calculator. ENI's president, Lloyd Ferguson, designed and prepared the programs to perform various functions including storage of information relating to student numbering, student progress, class information and scores. The programs could also produce reports on these topics. ENI incorporated specialized terminology and concepts into the automated recordkeeping system.[1]

In May 1979, ENI decided to develop a management program compatible with the new rapid low-cost program-

[1] A number of these specialized terms and concepts were incorporated by ENI into Project Basic, and then appeared in the defendants' program and manual.

mable microcomputers which had become increasingly available to ENI's customers. ENI envisioned that these programs would both facilitate basic accountability of school instructional curriculums and perform various collateral functions such as preparing progress reports, teacher/class reports, student report cards, school and district status reports, and so forth. To bring this vision to life, Ferguson wrote the system bid guidelines with programming specifications. This included flow diagrams and prepared numbering and coding systems. Ferguson also developed sample printouts and reports incorporating all of the concepts developed by ENI for computer-managed instruction.

In need of a computer programmer, ENI was referred to defendant Brian Brazda, the president and a partner of defendant Chicago Systems Software ("CSS").[2] James Davey, the other defendant, is vice-president and also a partner of CSS. CSS designs and sells computer software and provides custom programming services for microcomputers. CSS possessed the necessary programming skills to provide ENI the computer coding necessary to run the ENI Computer Managed Instruction Program on a Commodore computer. On June 21, 1979, ENI and CSS agreed that CSS would provide the necessary programming, including complete documentation of how the system operated, for $5,500 (to compensate CSS for an estimated 200 to 300 hours of programming work).

CSS and ENI set up a schedule that required CSS to begin working on ENI's program by July 11, 1979. CSS was to demonstrate the final version of the program during an in-service training session in Phoenix in mid-August of 1979. CSS began work on ENI's program in late June or early July of 1979. On August 6, 1979, Brazda received a letter from Ferguson setting out the "terms of this com-

[2] For convenience sake, we will refer to the defendants Brazda, Davey, and CSS corporately as "CSS" unless the context requires greater specificity.

mitment." One such term was that "[t]he ENI Copyright of this program is fully recognized by Chicago Software Systems [sic]." CSS completed the final program by mid-August, and on or about August 14, 1979, Davey and Brazda attended an ENI demonstration in Phoenix, where the new program was introduced to ENI customers. The new program was operational, but ENI's customers requested functional changes and corrections, which Davey and Brazda made. Following the demonstration in Phoenix, Brazda (on behalf of CSS) signed an "ENI Microcomputer Program Copyright Statement" prepared by Ferguson, which implemented Ferguson's letter of August 6.[3] After Brazda signed the statement, ENI paid CSS the first $1,500 of CSS's fee.

As soon as the new program became operational in April 1980, ENI began to market its computer-managed instruction program throughout the United States under the trade name "Project Basic." ENI also published a Project Basic user's manual. On June 13, 1980, ENI applied for and received copyright registration for the user's manual. The registration labelled the manual a "work made for hire," but omitted any date of publication. ENI printed a paper copyright notice on its manual.

In April 1980, CSS began to market its own program and user's manual entitled "Computerized Classroom Man-

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[3] The statement which Brazda signed provided:

ENI MICROCOMPUTER PROGRAM
COPYRIGHT STATEMENT

I the undersigned agree that all Microcomputer Programming done by Chicago Systems Software, 2200 W. Lawrence Avenue, Chicago, Illinois 60625 for Evans Newton Incorporated, hereinafter referred to as ENI, is the exclusive property of ENI. I agree not to sell, trade, give, or intentionally make available programs written for ENI to any private or public individual or corporation. I agree also that my employees should be informed of the above restriction and will take all reasonable precautions to prevent the illegal use of programs written for ENI.

agement." The new CSS program competed with the ENI Project Basic program. CSS demonstrated and distributed its program to various potential users and customers. CSS sold two complete copies of its program for $1,200. CSS also sold demonstration disks containing its program to three customers for less than $200.

Material portions of the CSS user's manual were substantially similar to ENI's Project Basic user's manual. Furthermore, material portions of CSS's program were similar both in form and function to material portions of ENI's Project Basic program. These similarities violated both the agreement between ENI and CSS and ENI's copyright. On or about June 13, 1980, counsel for ENI sent a letter to CSS maintaining that CSS was "attempting to sell an instructional management program that is basically the same" as the program CSS wrote for ENI. ENI demanded that CSS "immediately desist from any attempts to sell or otherwise make available to third parties any programs or material prepared for ENI or furnished [CSS] by ENI." ENI apparently also sent a copy of this letter to Richard Powers of Commodore Business Machine, a potential customer for CSS.

ENI's Project Basic program in its completed form includes both the computer software and the user's manual. The two components have little independent value. In 1980 ENI marketed Project Basic to approximately 300 Commodore computer dealers. Sixty of the Commodore dealers became Project Basic dealers. In return for exclusive Project Basic sales territories, the Commodore dealers paid ENI an amount ranging from $10,000 to $25,000, depending upon the size of the particular dealer's metropolitan area. Although ENI was unsuccessful in obtaining any Project Basic dealers in Georgia, Texas, Illinois, Wisconsin, Minnesota, Ohio, and Oklahoma, this failure was not due to confusion in the marketplace, as CSS also failed to obtain any dealers in those states. Between June of 1980 and June of 1982, no one besides CSS was marketing a program that competed with Project Basic.

Following a bench trial, the district court issued a decision on September 11, 1984, which the court subsequently amended on October 29, 1984. The district court found that CSS had infringed upon ENI's valid copyright for the Project Basic manual.[4] Alternatively, the court found that CSS engaged in acts of unfair competition and violated the parties' confidentiality agreement. The court enjoined CSS from further infringement and copying and ordered CSS "to deliver up all infringing articles for destruction." The court dismissed the counterclaims of CSS. The court found ENI's loss of profit damages (or statutory damages) to be $16,000. Because CSS acted knowingly, willfully, and intentionally, the court awarded ENI exemplary damages of $16,000. Finally, the court allowed ENI to recover its costs and attorneys' fees under copyright law. On February 27, 1985, the district court entered a final order awarding ENI $16,000 in attorneys' fees. ENI's bill of costs is evidently still pending and not an issue for this appeal.

II. DISCUSSION

The defendants raise numerous objections to the district court decision. CSS's principal argument is that ENI purposefully jumbled and obfuscated the facts and ENI's various legal theories in order to confuse the trial judge and conceal ENI's true motive for bringing the suit—to eliminate CSS as a competitor. More particularly, CSS alleges that (1) ENI failed to prove copyright infringement, (2) ENI failed to establish a factual or legal basis under contract, trade secret, confidentiality, or unfair competition theory for preventing CSS from marketing its program or manual, (3) ENI failed to demonstrate that it was entitled to injunctive relief, damages, costs, or attorneys' fees, and (4) the district court should not have

[4] The district court based this finding primarily upon viewing portions of the two software programs and hearing expert testimony on the issue of similarity.

dismissed CSS's counterclaim. We will address the defendants' four arguments in order.

A. Copyright Infringement

In *Selle v. Gibb*, 741 F.2d 896 (7th Cir. 1984), the court set out the four elements necessary to prove copyright infringement: "(1) ownership of the copyright in the complaining work; (2) originality of the work; (3) copying of the work by the defendant, and (4) a substantial degree of similarity between the two works." *Id.* at 900. Although *Selle* involved a musical composition, the four elements apply with equal force to the computer manual at issue here.

CSS claims that the plaintiff and defendants were co-authors and co-owners of the copyrighted work, and therefore CSS could not be an infringer. *See Richmond v. Weiner*, 353 F.2d 41, 46 (9th Cir. 1965), *cert. denied*, 384 U.S. 928 (1966). CSS argues that the district court erred when it determined that the plaintiff's manual was a "work made for hire." Under the Copyright Act of 1976, "copyright . . . vests initially in the author or authors of the work." 17 U.S.C. § 201(a) (1985). "In the case of a work made for hire, the employer or other person for whom the work was prepared is considered the author." *Id.* § 201(b). To constitute a "work made for hire," the work must be either (1) "prepared by an employee within the scope of his or her employment," or (2) "specially ordered or commissioned." *Id.* § 101. In order to have a "work made for hire" within the latter category, "the parties [must] expressly agree in a written instrument signed by them that the work shall be considered a work made for hire." *Id.* Because ENI produced no written instrument, CSS correctly asserts that the computer manual must fall within the "employee" category if it is indeed a "work made for hire."

ENI's copyright registration certificate for the manual described the manual as a "work made for hire," as did the district court's finding of fact. The district court also

found, however, that CSS was an "independent contractor." CSS argues that if it was an independent contractor the manual cannot fall within the employee category, and thus the manual was not a "work made for hire." Whether CSS was an employee of ENI for purposes of 17 U.S.C. § 101 turns upon whether Congress intended the term employee to encompass only "regular" employees as CSS contends, or whether Congress intended the 1976 Act to retain the somewhat more flexible definition of employee under the 1909 Copyright Act.

The Second Circuit faced this same issue recently in *Aldon Accessories v. Spiegel*, 738 F.2d 548 (2d Cir.), *cert. denied*, ____ U.S. ____ (1984). In *Aldon*, the court held that statuettes designed by artists and artisans who were not regular employees of the copyright holder could fall within the "work made for hire" doctrine where the contractors operated under the supervision and direction of the copyright holder.[5] *Id.* at 551-53. The court found that the proper issue was not, as CSS maintains, whether the defendant was an employee or an independent contractor, but rather "[was] the contractor 'independent' or [was] the contractor so controlled and supervised in the creation of the particular work by the employing party that an employer-employee relationship exist[ed]." *Id.* at 552. In reaching this conclusion, the *Aldon* court carefully considered the legislative history of 17 U.S.C. § 101 and

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[5] At issue in *Aldon* was the following instruction, which the court held to be an accurate expression of the law:

> A work for hire is a work prepared by what the law calls an employee working within the scope of his employment. What that means is, a person acting under the direction and supervision of the hiring author, at the hiring author's instance and expense. It does not matter whether the for-hire creator is an employee in the sense of having a regular job with the hiring author. What matters is whether the hiring author caused the work to be made and exercised the right to direct and supervise the creation.

738 F.2d at 551.

determined that Congress did not intend to significantly narrow the definition of "employee" as CSS here contends. The court concluded that nothing in the 1976 Copyright Act or its legislative history indicated "that Congress intended to dispense with . . . prior law [the 1909 Copyright Act and cases construing it]" which held that "if an employer supervised and directed the work, an employer-employee relationship could be found even though the employee was not a regular or formal employee." *Id.* We find the Second Circuit's analysis and conclusion compelling.

Having properly framed the issue, it is clear that the district court's finding that the manual was a "work made for hire" is not clearly erroneous. The evidence at trial essentially came down to a credibility contest. The judge believed ENI's testimony that Ferguson supervised and directed the work, and that CSS merely used their programming skills to produce the work according to ENI's specifications. ENI therefore established the first element of its copyright claim—that ENI owned the sole copyright in the disputed work. *Selle*, 741 F.2d at 900.

CSS also alleges that ENI failed to prove the second and third elements of copyright infringement, *i.e.*, the originality of the Project Basic manual and the copying of the manual by CSS. CSS does not clearly develop these arguments, but both appear predicated upon CSS's mistaken claim that it was a coauthor of all the work it did for ENI. These claims are without merit. ENI produced enough evidence on each element to support the district court's decision.

CSS argues that ENI's copyright infringement claim must ultimately fail because "there is no similarity between plaintiff's manual and defendants' program or manual." To determine substantial similarity, we look at (1) whether the defendant copied from the plaintiff's work and (2) whether the copying went so far as to constitute an improper appropriation. *Scott v. WKJG*, 376 F.2d 467, 469 (7th Cir.), *cert. denied*, 389 U.S. 832 (1967). The test

for substantial similarity is "whether the accused work is so similar to the plaintiff's work that an ordinary reasonable person would conclude that the defendant unlawfully appropriated the plaintiff's protectible expression by taking material of substance and value." *Atari, Inc. v. North American*, 672 F.2d 607, 614 (7th Cir.), *cert. denied*, 459 U.S. 880 (1982). *See also Ideal Toy Corporation v. Fab-Lu Ltd.*, 360 F.2d 1021, 1022 (2d Cir. 1966).

In this case, the district court found that ENI's Project Basic program included both the computer software and the user's manual, and the two components had no significant value independent of one another. The manual is, in essence, an explanation of the program and a description of what the user will see on the screen while operating the program. Brazda, one of the defendants, acknowledged that CSS contracted to provide ENI with a manual for use with Project Basic. The manual was largely useless apart from the program.

The testimony of ENI's president Ferguson established the similarities of expression between the two manuals, and this testimony is sufficient to support the district court's finding. Moreover, ENI buttressed Ferguson's testimony with substantial evidence about the similarities between the two underlying programs upon which the manuals were based.[6] This factual dispute turned upon

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[6] We do not express any opinion as to whether the substantial evidence of the similarity of the underlying programs would be sufficient by itself. This evidence is clearly probative, however, because the program is the basis for the manual, and the program and the manual are intertwined as the final product.

This case is unusual because ENI's evidence of substantial similarity focused primarily on the computer programs and not the manuals. ENI brought infringement claims on both the program and the manual, but at trial ENI did not have the proper documents to prove it had registered its copyright for the program, so the district court was forced to dismiss the program claim. This left ENI with only its claim that CSS infringed the copyright on the Project Basic manual.

the district judge's in-court evaluation of the manuals, the credibility of the witnesses, and expert testimony, and we do not find that his decision was clearly erroneous. Therefore, we affirm the district court's finding that CSS infringed ENI's copyright in the Project Basic manual.

B. Contract, Trade Secret, Confidentiality, and Unfair Competition.

The district court also found that CSS was liable to ENI under several alternate theories. The court held CSS had engaged in acts of unfair competition and violated the confidentiality agreement between the parties. Because these alternate theories are merely additional grounds to support the court's decision, in view of our holding that CSS infringed ENI's valid copyright in the Project Basic manual, it is unnecessary for us to review the district court's resolution of the alternate theories.

C. Relief

The district court granted an injunction against further infringement and copying, and required CSS to deliver up all infringing articles for destruction. The court awarded ENI damages of $16,000, apparently either measured by ENI's loss of profits, 12 U.S.C. § 504(b) (actual damages), or as statutory damages pursuant to 17 U.S.C. § 504(c). Because CSS's actions were "knowing, willful, and intentional," the court awarded ENI $16,000 in punitive damages. Finally, the court allowed ENI to recover its attorneys' fees and costs under copyright law. The court later set the amount of attorneys' fees at $16,000. CSS challenges each component of the district court's relief order. To the extent that CSS bases its challenges upon its argument that it did not infringe ENI's copyright (*e.g.*, CSS's claim that ENI did not establish a basis for injunctive relief), we need not consider the challenges. CSS raises an additional argument that even if some basis of liability was proven, ENI did not prove actual damages of $16,000. Our analysis of this issue is complicated by

the fact that the district court did not make it clear whether the damages were actual or statutory, or what the basis for the $16,000 amount was. Nevertheless, we find sufficient evidence in the record to hold that the district court did not err in awarding $16,000 to ENI.

CSS contends that its total sales of the infringing program were only $1,400, and that ENI failed to show that CSS sold its manual or program to anyone that ENI would have sold to, or that CSS's sales efforts caused any confusion, or that CSS caused ENI to lose any sales. ENI counters that it presented sufficient evidence of market penetration, dollar volume, and franchise and dealer fees which indicated that the $16,000 award was justified, if not overly conservative. ENI points out that the mere fact that CSS was not able to capitalize as it had hoped on its infringement does not prevent the district court from compensating ENI for lósses sustained in excess of CSS's profit.[7]

ENI presented sufficient evidence to support the district court's award of $16,000. Commodore dealers paid ENI between $10,000 and $25,000 for exclusive sales territories in which to market Project Basic. Ferguson testified that ENI had an overall market penetration of approximately 20% but was unable to make a single sale within the midwest region in which CSS was operating. Ferguson further testified that in his opinion ENI's sales of Project

[7] In Finding of Fact #22, the district court found that "ENI suffered damages for the actual dealer sales or licenses made by CSS," an amount which the court recognized the parties had stipulated to being approximately $1,400. The court went on to find that "the total amount of plaintiff's loss attibutable to defendants' wrongful acts is not more than $16,000.00." The defendants claim that the court contradicted itself, but we believe it more likely that the court intended "the total amount of plaintiff's loss" to include more than just the damages for CSS's sales. In Finding of Fact #22, the court referenced back to *both* Finding of Fact #15 (the parties' stipulation to approximately $1,400) and Finding of Fact #19, which discussed Project Basic's market penetration and the licensing of Commodore dealers.

Basic, although they increased substantially each year, would have grown even more rapidly but for CSS's infringement.[8] The district court evidently gave some weight to Ferguson's testimony, although the court clearly did not grant ENI the substantial damages suggested by Ferguson. Rather the district court chose a more modest estimate, perhaps based upon what ENI would have profited had one Commodore dealer in the midwest purchased an exclusive sales territory ($10,000 to $25,000 depending upon the size of the metropolitan area). The record contains sufficient support for us to find that the district court did not err in awarding $16,000 was not clearly erroneous.

The district court also assessed $16,000 in punitive damages against CSS and $16,000 to reimburse ENI's attorneys' fees. CSS argues the district court erred in basing these two decisions upon copyright law because 17 U.S.C. § 412 prohibits the award of statutory damages (which would include punitive damages) or attorneys' fees unless the plaintiff registers its copyright prior to the infringement.[9] *See Deltak, Inc. v. Advanced Systems*, 767 F.2d

[8] The defendants claim that the district court excluded all the evidence plaintiff relies upon to support damages in excess of $1,400. Although the transcript is far from clear, we read it as indicating that what the district court disallowed was the plaintiff's attorney's attempt to solicit from Ferguson an estimate of how many Commodore dealers ENI would have licensed but for CSS's infringement. The court did not exclude ENI's evidence (most of which was merely a repeat of previously introduced testimony), but rather ruled that the evidence was an insufficient foundation for the ultimate question to Ferguson. The confusion in the record apparently stems from the court's use of "offer of proof" to describe ENI's summary and repeat of evidence already in the record, evidence which ENI claimed laid the necessary foundation to allow it to ask Ferguson the ultimate question.

[9] 17 U.S.C. § 412 provides:

> In any action under this title, other than an action instituted under section 411(b), no award of statutory damages or of attorney's fees, as provided by sections 504 and 505, shall be made for—

(Footnote continued on following page)

357, 359 (7th Cir. 1985). The district court found that CSS began its infringement in April 1980, and ENI applied for and received its copyright registration in June 1980. ENI failed to offer any argument, in either its brief or at oral argument, why section 412 should not apply. Therefore, ENI is limited to recovering its actual damages for CSS's infringement pursuant to 17 U.S.C. § 504(b).

In awarding ENI $16,000 in attorneys' fees and an as yet undetermined amount for costs, the district court specifically linked the award to copyright law. The district judge said that under Illinois law, which governed ENI's breach of contract theory, a plaintiff cannot receive attorneys' fees for breach of contract. Because the district court erred in awarding fees based upon copyright law in violation of 17 U.S.C. § 412, we must reverse the court's award of fees.

The district court's award of $16,000 in punitive damages is more troublesome because the court failed to specify which ENI theory or theories supported punitive damages. The court merely based the punitive damages on CSS's "knowing, willful and intentional" actions. Under copyright law, punitive damages could come from an award of statutory damages for willful infringement. 17 U.S.C. § 504(c)(2). Statutory damages are subject to the same 17 U.S.C. § 412 limitation as attorneys' fees, however—the plaintiff must register the copyright prior to the infringement. As we pointed out above, the district court found that ENI did not register its copyright prior to CSS's infringement. Therefore, ENI cannot justify punitive damages under copyright law. Because ENI fails to articulate any alternative ground to uphold the district

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[9] *continued*

(1) any infringement of copyright in an unpublished work commenced before the effective date of its registration; or

(2) any infringement of copyright commenced after first publication of work and before the effective date of its registration, unless such registration is made within three months after the first publication of the work.

court's decision, we must reverse the court's award of punitive damages.

D. CSS's Counterclaims

CSS's final argument is that the district court violated Fed. R. Civ. P. 52 by dismissing CSS's counterclaims with prejudice after the trial without any findings of fact or conclusions of law. CSS had counterclaimed for inducement to breach contract, unfair competition, and trade libel. The counterclaims arose from ENI's attempts to protect itself against CSS's infringement of ENI's copyright. Inasmuch as the counterclaims were based upon CSS's theory of the case (*i.e.*, that neither CSS's manual nor program infringed ENI's copyright), a theory which we decline to embrace, the district court did not err in dismissing CSS's counterclaims. The findings of fact and conclusions of law concerning ENI's claims, which were set out in the district court's memorandum, clearly support the dismissal of CSS's counterclaims.

III. CONCLUSION

The district court found that CSS infringed upon ENI's copyright in the user's manual for Project Basic, an ENI educational-recordkeeping computer program for which CSS did the programming. We affirm the district court's grant of an injunction and $16,000 in actual damages to ENI. We reverse the court's award of attorneys' fees and punitive damages because both are barred by 17 U.S.C. § 412. The district court's judgment is therefore

AFFIRMED IN PART, REVERSED IN PART.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

United States District Court

EVANS NEWTON, INC.

Plaintiff

v.

CHICAGO SYSTEMS SOFTWARE, et al

Defendants

DISTRICT NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

DOCKET NUMBER
81 C 3564

NAME OF JUDGE
THOMAS R. MC MILLEN

IT IS ORDERED AND ADJUDGED

That plaintiff has a valid and enforceable copyright in this action, and defendants are found to have committed acts of infringement. Plaintiff is granted an injunction against further infringement and copying . . . Defendants' counterclaim is dismissed with prejudice. Judgment is entered for plaintiff against defendants for $16,000. Exemplary damages are awarded in the amount of $16,000. Plaintiff may recover its costs and attorneys fees incurred in this action under copyright law. . .

DATE
Sept. 11, 1984

STUART CUNNINGHAM

DEPUTY CLERK
KATHLEEN BRANCH

UNITED STATES DISTRICT COURT,
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

Name of Presiding Judge, Honorable THOMAS R. McMILLEN

Cause No. 81 C 3564 Date OCT. 29, 1984

Title of Cause EVANS NEWTON INC. v. CHICAGO SYSTEMS SOFTWARE et al.

Reserve space below for notations by minute clerk

The court will grant whatever corrections or modifications plaintiff has agreed to concerning defendants' motion to amend our decision of Sept. 11, 1984. To the extent defendants other proposed changes or additions tend to change the merits or ultimate result, they are overruled and plaintiff's objections are sustained. (Decision attached)

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

EVANS NEWTON INC.,
Plaintiff,

vs.

CHICAGO SYSTEMS SOFTWARE, et al.,
Defendants.

NO. 81 C 3564

DECISION

Defendants have filed a timely motion to amend our decision of September 11, 1984, and plaintiff has filed a response thereto, concurring in some of the objections. Plaintiff was the partially prevailing party in this case, and therefore we will grant whatever corrections or modifications it has agreed to. This includes the second sentence of Finding No. 5, the amendment to the first sentence of Finding No. 6, the expansion of the last sentence of Finding No. 8, the revision of the sentence structure in Finding No. 12, the change of the document identification in the last sentence of Finding No. 13, the more specific date in Finding No. 14, and the addition of a sentence to Finding No. 17.

To the extent that the defendants other proposed changes or additions to our decision of September 11, 1984 tend to change the merits or ultimate result, they are overruled and plaintiff's objections are sustained. Specifically, Finding No. 19 is supported by the weight of the evidence, and Finding No. 22 is a reasonable inference based upon the weight of the evidence. The measure of the amount of attorney's fees to be awarded will be

considered when a petition for them has been filed, controlled by the principles of *Hensley v. Eckerhart*, ____U.S. ____, 103 S.Ct. 1933 (1983).

ENTER:

/s/ THOMAS R. MCMILLEN
JUDGE, UNITED STATES DISTRICT COURT

DATED: OCT 29 1984

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

EVANS NEWTON INCORPORATED
Plaintiff,

vs.

CHICAGO SYSTEMS SOFTWARE, BRIAN BRAZDA, and JAMES DAVEY, d/b/a Chicago Systems Software,
Defendants.

NO. 81 C 3564

FINDING OF FACT

1. This is an action for infringement of United States Copyright arising out of the Copyright Act 17 U.S.C. §1 *et seq.*, and for a substantial and related claim of unfair competition and breach of contract. Jurisdiction and venue are based upon 28 U.S.C. §§1338 and 1400(a).

2. Plaintiff, Evans Newton Incorporated (ENI), is a corporation duly incorporated under the laws of New Jersey having its principal place of business at 7650 E. Redfield Road, Suite 5D, Scottsdale, Arizona.

3. Defendant, Chicago Systems Software (CSS) is an unincorporated business having its business location at 2200 W. Lawrence Avenue, Chicago, Illinois, 60625. Defendant, Brian Brazda is the president and a partner of defendant CSS and resides in Indianhead Park, Illinois. Defendant James M. Davey is the vice-president and partner of the defendant CSS and resides in Chicago, Illinois. CSS designs and sells software and provides custom programming services for microcomputers and was established in 1979.

4. This Court has jurisdiction over the parties.

5. Plaintiff was incorporated in 1973 for the purpose of providing recordkeeping systems to educational institutions throughout the country. During 1978, in order to adapt its educational instructional program to programmable calculators ENI developed in cooperation with Victor Business Products, calculator managed and assisted programs for use with the Victor

4900 programmable calculator. The programs were designed and prepared by ENI's president Lloyd Ferguson and performed various functions including storage of information relative to student numbering, student progress, class information and scores, and producing reports on the same topics. Incorporated in the automated record keeping system developed by ENI in 1978 were specialized terminology and concepts, such as "teacher judgment", "teacher recommendation", "coding systems for tracking of subject and grade level", "student course of studies", "student card", "diagnostic test". (Plaintiff's Exhibit 37).

6. With the advent of new rapid low-cost programmable microcomputers, ENI set out in about May 1979 to develop a management program compatible with these new computers for performing and achieving basic accountability of school instructional curriculums and for performing various functions including preparation of progress reports, grouping reports, teacher/class reports, student report cards, school and district status reports and the like. (Stipulated Fact G)

7. In connection with the computer managed instruction programs, Mr. Ferguson wrote system bid guidelines with programming specifications including flow diagrams; prepared numbering and coding systems; developed sample printouts and reports incorporating all of the concepts developed by ENI for computer managed instruction. (Plaintiff's Exhibit 31)

8. ENI was then referred to Brian Brazda and CSS who could provide the computer coding necessary to operate the ENI Computer Managed Instruction Program on a Commodore computer. On June 21, 1979 CSS agreed to provide the programming, including complete documentation for the operation of the system, for a total price of Five Thousand Five Hundred Dollars for 200 to 300 hours of programming work ($5,500.00). (Stipulated Fact I; Plaintiff's Exhibits 1 and 23)

9. Unbeknownst to plaintiff, Mr. Brazda had obtained listings and cassette programs from a former co-worker at Victor Business Products, Don Cawthorne, early in 1979. (Defendants' Exhibits V, W, X.) These materials comprised source code listings and a cassette tape for a skeleton computer program for a classroom management and testing program in the C BASIC

language on a microcomputer. Mr. Cawthorne had begun to convert this program to a Commodore computer and developed a version of his program on tape for the Commodore computer, but he gave all of these materials to Mr. Brazda when Mr. Cawthorne began to work for Commodore directly. These materials were used by CSS to develop its own versions of a classroom management program in about April 1979 (Defendants' Exhibits L, M) and was the primary source for its demonstration version of such a program (Defendants' Exhibit O; Stipulation H). This had been shown to Ferguson and his customers on or about May 3, 1979 by Brazda, without restrictions.

10. The "critical path schedule" established by the parties required that CSS begin working on the ENI program by July 11, 1979 and that the final version of the program be demonstrated by CSS during an in-service training session in Phoenix in mid-August, 1979 (Plaintiff's Exhibit 2). CSS began this work by late June or early July 1979. On August 6, 1979, Mr. Ferguson wrote to Mr. Brazda setting forth "terms of this committment", including: "6. The ENI Copyright of this program is fully recognized by Chicago Software Systems [sic]" (Plaintiff's Exhibit 23). The final programs were completed by CSS by mid-August, and on or about August 14, 1979, defendants Davey and Brazda attended an ENI demonstration in Phoenix, Arizona to introduce the programs to ENI customers. CSS' travel expenses of about $1,000 were paid by CSS. The program was operable, but functional changes were requested by the customers, and defendants Davey and Brazda made these changes and corrections Stipulated Fact J; Brazda testimony).

11. At the end of the demonstration in Phoenix, Mr. Brazda signed an "ENI Microcomputer Program Copyright Statement" prepared by Mr. Ferguson which Mr. Brazda signed on behalf of CSS and which stated as follows (Plaintiff's Exhibit 38):

ENI MICROCOMPUTER PROGRAM
COPYRIGHT STATEMENT

> I the undersigned agree that all Microcomputer Programming done by Chicago Systems Software, 2200 W. Lawrence Avenue, Chicago, Illinois 60625 for Evans Newton Incorporated, hereinafter referred to as ENI, is the exclusive property of ENI. I agree not to sell, trade, give, or intentionally make available programs written for ENI to any private or public individual or corporation. I agree also that my employees should be informed of the above restriction and will take all reasonable precautions to prevent the illegal use of programs written for ENI.

Mr. Ferguson testified that the above "Copyright Statement" was the implementation of ¶6 of his August 6, 1979 letter. After the statement was signed, CSS was paid the first $1500 of its fee.

12. After the system was made operational, ENI marketed its computer managed instruction program under the trade name "Project Basic" beginning in April 1980, and ENI marketed the program in many parts of the United States.

13. ENI published a users manual entitled "Project Basic" in 1980. On June 13, 1980, ENI applied for and received registration of the manual by Certificate of Copyright Registration No. TX-U-46154. This registration states that the manual is a "work made for hire" but omits any date of publication. (Stipulated Fact O; Plaintiff's Exhibit 7) A proper copyright notice was printed on the ENI manual, according to Mr. Ferguson, and one appears as Plaintiff's Exhibit 7.

14. Beginning in April 1980, CSS marketed a program and users manual entitled "Computerized Classroom Management." The CSS program is competitive to the ENI program and users manual which was developed by and for ENI. The CSS program and manual were demonstrated and distributed to various potential users and customers at two or three dealer meetings. (Stipulated Fact P)

15. CSS sold two (2) complete copies of its program for a total of One Thousand Two Hundred Dollars ($1,200.00). Demonstration discs containing the CSS/CCM program were also sold to three customers for which CSS received less than Two Hundred Dollars ($200.00). (Stipulated Fact R)

16. Material portions of the defendants' manual have substantial similarity to plaintiff's manual. Material portions of the defendants' computerized classroom management software program have this similarity in both form and function to material portions of the plaintiff's program. This violated the agreements between the parties (¶¶10 and 11, *supra*) and also violated plaintiff's copyright (¶13, *supra*). The court makes this finding after viewing portions of the foregoing programs and hearing expert testimony on the issue of similarity.

17. On or about June 13, 1980, counsel for ENI sent a letter to CSS claiming that CSS was "attempting to sell an instructional management program that is basically the same" as the one it wrote for ENI; and demanding that CSS "immediately desist from any attempts to sell or otherwise make available to third parties any programs or material prepared for ENI or furnished you by ENI." (Stipulated Fact S) A copy of this letter was sent to Richard Powers of Commodore Business Machine, a potential customer for defendants' program.

18. ENI's project basic program includes both the computer software and the published users manual. The two components have no significant value independent of one another. (Ferguson testimony; Brazda testimony)

19. Beginning in mid-1980, Lloyd Ferguson, on behalf of ENI, marketed Project Basic by contacting Commodore computer dealers which totaled approximately three hundred (300). Sixty (60) Commodore Dealers became ENI dealers for Project Basic. In return for exclusive sales territories, those Commodore dealers who agreed to become dealers for ENI's Project Basic paid ENI between Ten Thousand ($10,000.00) and Twenty Five

Thousand Dollars ($25,000.00), depending on the size of the metropolitan area which each dealer served.

20. ENI made efforts to sell its program to approximately sixty (60) Commodore dealers in the states of Georgia, Texas, Illinois, Wisconsin, Minnesota, Ohio and Oklahoma. ENI did not acquire any licensee dealers for Project Basic in these areas, but this was not shown to be due to confusion in the marketplace caused by the defendants' program and manual. Defendants did not obtain dealers in those areas either. (Ferguson and Stewart testimony)

21. No competitive programs other than those marketed by ENI and CSS were shown to have existed in the period of June 1980 to June 1982.

22. Based upon the market share and penetration of CSS and its sales volume throughout the United States, ENI suffered damages for the actual dealer sales or licenses made by CSS. The total amount of plaintiff's loss attributable to defendants' wrongful acts is not more than $16,000.00, based on findings 15 and 19, *supra*.

CONCLUSIONS OF LAW

1. This Court has jurisdiction of the parties and of the subject matter and the issues herein involved. Venue is properly in this district as to all defendants.

2. Plaintiff is the owner of Copyright Registration No. TX-U-46154 and, against defendants, is the owner of all rights in the ENI/CMI manual designated "Project Basic." The manual is a "work made for hire" within the meaning of 17 U.S.C. §101.

3. Both the ENI/CMI software and manual constitute a "tangible medium of expression" which can be perceived, reproduced or otherwise communicated within the meaning of 17 U.S.C. §102(a). The ENI/CMI software and the manual both attain the level of creativity required under the Copyright Code and are susceptible to copyright protection. *Apple Computer, Inc. v. Formula International, Inc.*, 725

F.2d 521 (9th Cir. 1984).

4. The ENI/CMI software and manual were created after January 1, 1978 and are subject to the 1976 Copyright Act.

5. The ENI manual was originally registered by plaintiff as an unpublished work under Copyright Registration No. TX-U-46154 and was subsequently published in 1980. As owner, plaintiff's protection is not defeated by the fact that some of the material may have been originated by another person and had been published before it was registered by plaintiff. 17 U.S.C. §408(a) and §410(c).

6. The instructions and specifications and other materials given to CSS by ENI to enable CSS to assist in the programming constitute an ENI trade secret and were protected by the agreement between the parties.

7. In a partnership, the individual partners are jointly and severally liable for the conduct of the partnership.

8. The law permits the owner of a trade secret to make his secret known to others subject to the contractual duty not to disclose the secret. *Allen Qualley Co. v. Shellmar Prods.*, 31 F. Supp. 293 (N.D. Ill.), aff'd 36 F.2d 623 (7th Cir. 1929).

10. Defendants have breached the contract existing between the parties.

11. Under Illinois law, the unprivileged use or disclosure of plaintiff's trade secrets creates liability if the disclosure or use constitutes a breach of confidence reposed in the defendant by plaintiff. *Jones v. Ulrich*, 342 Ill. App. 16 (3d Dist. 1950).

12. A contractual prohibition to hold in secret information imparted to one in employment is breached by use of that information regardless of whether the information is a trade secret. *Lear Siegler, Inc. v. Ark-Ell Springs, Inc.*, 569 F.2d 286 (5th Cir. 1978); see also *DuPont de Nemours Powder Co. v. Masland*, 244 U.S. 100 (1917).

13. Trade secrets disclosed by a manufacturer to an independent contractor in connection with services to be performed by the latter constitutes confidential disclosure. *Jones v. Ulrich*, *supra*, conclusion 11.

14. Misappropriation results from the unauthorized use of a trade secret as evidenced by a comparison of the programs, as in this case. *Structural Dynamics Research Corp. v. Engineering Mechanics Research Corp.*, 401 F.Supp. 1102 (E.D. Mich. 1975).

15. Under Federal copyright law, the appropriate test for determining whether substantial similarity is present is whether an average lay observer would recognize the alleged infringing copy as having been appropriated from the substance of the protected work. See *Atari, Inc. v. North American, Etc.*, 672 F.2d 607, 614 (7th Cir. 1982); *Ideal Toy Corp. v. Fab-Lu Ltd., Inc.*, 360 F.2d 1021, 1022 (2d Cir. 1966). Here, the court as an average lay observer did recognize the defendants' program as having been appropriated from the plaintiff's protected work.

16. In this case defendants were independent contractors retained because of their pre-existing expertise in the field of educational programs. Plaintiff's letter of August 6, 1979 (Finding 10) cannot prevent defendants from utilizing their expertise after termination of their relationship with plaintiff. However, it does preclude them from using the materials in the form delivered to them by ENI and in the language developed for ENI, even though defendants already had similar materials. See *Apple Computer, Inc. v. Formula International, Inc.*, *supra*, conclusion 4, at p. 525.

17. Misappropriation of a source code occurs where there is substantial similarity in the overall structure, function, organization and segments of code which were solely arbitrary. *Structural Dynamics Research Corp. v. Engineering Mechanics Research Corp.*, *supra*, conclusion 4.

18. The defendants in their CSS/CMI operators

manual copied and included substantial and material portions of the plaintiff's copyrighted works in violation of the exclusive rights of the copyright owner defined in 17 U.S.C. §106. *Wilson v. Haber Bros.*, 275 F. 346 (2d Cir. 1921).

19. The expression or display of software from a ROM or disk onto paper or a video screen is a reproduction within the definition of 17 U.S.C. §106. *Midway Mfg. Co. v. Strohon*, 564 F.Supp. 741 (N.D. Ill. 1983).

20. The sale of software by the owner, including code which is protected, is not a sale or disclosure which terminates trade secret protection. cf. *Midway Mfg. Co. v. Strohon, supra.*

21. An ENI manual, relating to an educational program for the Victor 4900 programmable calculator, carried a presumptively valid copyright notice, but plaintiff did not produce a certificate of registration for this document and it is not enforceable in this action. 17 U.S.C. §410(c).

22. The defendants' activities in reproducting [sic] portions of the plaintiff's software and manual do not constitute a fair use within 17 U.S.C. §107.

23. Defendants are liable as copyright infringers of the manual Project Basic under 17 U.S.C. §501. Plaintiff is entitled to injunction under 17 U.S.C. §502. Plaintiff is also entitled to its actual damages under 17 U.S.C. §504. As its option, plaintiff may be entitled to statutory damages pursuant to 17 U.S.C. §504(c). Attorneys fees to the prevailing party are discretionary under 17 U.S.C. §505.

24. Plaintiff is entitled to judgment:

A. Plaintiff's copyright for the Project Basic manual is valid and enforceable in this action, and the defendants by selling a substantial copy of the CSS/CMI software program have committed acts of infringement.

B. Alternatively, defendants have engaged in acts of unfair competition and have violated the confidentiality agreement between the parties.

C. Plaintiff is granted an injunction against further infringement and copying.

D. Defendants are required to deliver up all infringing articles for destruction.

E. Defendants' counterclaim is dismissed with prejudice.

F. Plaintiff's damages are measured by plaintiff's loss of profit, or in the court's discretion, plaintiff is entitled to statutory damages. *Woolworth Co. v. Contemporary Arts, Inc.*, 344 U.S. 228 (1952). Judgment is entered for plaintiff against defendants for $16,000.

G. Defendants' actions were knowing, willful and intentional resulting in an award of exemplary damages in the amount of $16,000.

H. Plaintiff may recover its costs and attorneys fees incurred in this action, under copyright law. However, under Illinois law plaintiff is not entitled to attorney's fees for breach of contract, and Illinois law applies in this case. *American National Bank and Trust Co. v. Weyerhaeuser Co.*, 692 F.2d 455 (7th Cir. 1982); *George v. Haas*, 311 Ill. 382 (1924).

I. The defendants, and each of them, are jointly and severally liable to the plaintiff.

ENTER:

/s/ THOMAS R. MCMILLEN
JUDGE, UNITED STATES DISTRICT COURT

DATED: September 11, 1984

United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

July 16, 1986.

Before

Hon. WALTER J. CUMMINGS, Chief Judge
Hon. HARLINGTON WOOD, JR., Circuit Judge
Hon. RICHARD D. CUDAHY, Circuit Judge

EVANS NEWTON INCORPORATED, a New Jersey corporation,

Plaintiff-Appellee,

vs.

CHICAGO SYSTEMS SOFTWARE, and BRIAN BRAZDA, an individual, and JAMES M. DAVEY, an individual, d/b/a CHICAGO SYSTEMS SOFTWARE,

Defendants-Appellants.

No. 84-2971, 85-1359

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

No. 81 C 3564

Thomas R. McMillen
Judge.

ORDER

The opinion in this case, issued June 19, 1986, is amended to include the following additional case number:

85-1359.

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LAFF, WHITESEL, CONTE & SARET